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No. 94-888

IN THE
Supreme Court of the United States
OCTOBER TERM, 1994

NATIONSBANK OF TEXAS, N.A.,
Petitioner,

v.

JOHN GARAMENDI, INSURANCE COMMISSIONER OF THE STATE OF CALIFORNIA, IN HIS CAPACITY AS LIQUIDATOR OF EXECUTIVE LIFE INSURANCE COMPANY, *et al.*,
Respondent.

On Petition for Writ of Certiorari to the California Court of Appeal, for the Second Appellate District, Division One

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RESPONDENT'S BRIEF IN OPPOSITION

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COUNTERSTATEMENT OF QUESTIONS PRESENTED

The issue in this case is:

> whether the California Court of Appeal erred in its application of state contract law in a private dispute to conclude that an agreement by which the FDIC assigned one bank's trust business to another bank did not transfer any federal governmental priority.

Should certiorari be granted, Respondent would present two additional questions which were identified but not decided by the California Court of Appeal. These further questions are:

> whether the FDIC itself is entitled to federal governmental priority under 31 U.S.C. § 3713 (see Pet. App., 8a); and
>
> whether any United States government priority rights under 31 U.S.C. § 3713 may be assigned to non-governmental parties (see Pet.App., 12a, n.8).

RULE 29.1 STATEMENT

Pursuant to Rule 29.1 of the Rules of this Court, John Garamendi, Insurance Commissioner of the State of California, files this brief in his capacity as Liquidator and Trustee of Executive Life Insurance Company and the trust created by Order of the Superior Court of the State of California, County of Los Angeles. Executive Life Insurance Company's only subsidiary company, other than wholly-owned subsidiaries, is Flora Real Estate Management Company, which is an asset of the Executive Life Insurance Company Trust.

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RESPONDENT'S BRIEF IN OPPOSITION

JURISDICTION

There is no jurisdiction to review the Court of Appeal's decision because it rests on adequate state grounds of substantive contract law. This Court has no jurisdiction to review a state law ruling below resting on adequate and independent state grounds. 28 U.S.C. § 1257; *Herb v. Pitcairn*, 324 U.S. 117, 125 (1954).

The decision below turned solely on state law issues of contract interpretation. The Court of Appeal based its decision on the separate and independent ground that, on the facts and equities of this case, no contractual assignment of any asserted federal priority rights had been made to Petitioner. (Pet.App., 11a-21a). No United States government entity is a party to the contract here or

a party to this case. The contract in question provided, by its terms, that state law governs its interpretation and construction when, as here, there is no controlling federal law. (Purchase and Assumption Agreement § 13.4, Pet. App., 27a). As explained further in the Reasons For Denying The Petition, Part II.A., *infra*, there is no federal issue nor a basis to create "federal common law" in this case. This Court should therefore deny the Petition for lack of jurisdiction.

ADDITIONAL PERTINENT STATUTORY PROVISIONS

California Insurance Code § 1033 governs the priority distribution of the assets of an insolvent insurance company and provides:

> (a) Claims allowed in a proceeding under this article shall be given preference in the following order:
>
> (1) Expense of Administration.
>
> (2) Unpaid charges due under the provisions of Section 736.
>
> (3) Taxes due to the State of California.
>
> (4) Claims having preference by the laws of the United States and by laws of this State.
>
> (5) All claims of the California Insurance Guarantee Association, the California Life Insurance Guarantee Association, . . . and associations or entities performing a similar function in other states, together with claims for refund of unearned premiums and all claims of policyholders of an insolvent insurer that are not covered claims. . . .
>
> (6) All other claims.

COUNTERSTATEMENT OF THE CASE

Petitioner NationsBank of Texas, N.A. ("NationsBank"), as indenture trustee for certain taxable municipal bondholders, is the current holder of a Municipal Guaranteed Investment Contract ("Muni-GIC") issued by

Executive Life Insurance Company ("ELIC"). Although Petitioner portrays itself as a guardian of the federal banking system, its assertion of governmental status seeks to use the happenstance of the failure of the prior trustee bank in order to vault to the front of the line among ELIC's 350,000 policyholders. The result, if Petitioner were successful, would be that Petitioner—and thereby the investors in one particular municipal bond offering—would be fully paid their $295 million claim before, and at the expense of all other creditors, including life insurance policyholders, state guarantee associations, pension annuitants, structured settlement annuitants, and even other Muni-GIC trustees and their bondholders. (See Pet.App., 4a, 6a-8a).

The background facts of this case are correctly stated in the decisions of the Superior Court, Los Angeles County (Pet.App., 17a-18a, 19a-21a), and the Court of Appeal (Pet.App., 4a-8a). However, because the decision below relied on the language of the purchase and assumption contract by which Petitioner acquired the trust business in question, special attention to that language is warranted. The purchase and assumption agreement did not provide an assignment of any governmental priority rights. Indeed, there is no evidence that Petitioner believed or understood that it obtained any priority greater than that held by the failed bank.[1] The language in the agreement assigned particular assets of the failed bank:

> The Assuming Bank hereby accepts from the Receiver an assignment of, and the Receiver hereby sells, assigns, transfers, conveys and delivers to the Assuming Bank, all right, title and interest of the

[1] There was no legal basis for Petitioner to expect governmental priority at the time it entered the agreement. At that time, decisional law suggested—as it still does—that the FDIC itself was not entitled to governmental priority, and thus had no rights to assign. See Reasons For Denying The Petition, Part III, *infra*, at 21-25.

> Receiver *in and to all of the following assets of the [Failed] Bank* . . . .

(Pet.App., 24a) (emphasis added).[2] The listed assets assigned included the failed bank's "trust business," which included trusteeship of this Muni-GIC. (Pet.App., 24a-25a). More specifically, Petitioner's contract contained a section entitled "Agreement with Respect to Trust Business" that provided that "[t]he trust business of the bank is hereby transferred to the Assuming Bank effective as of [the] Closing" (Pet.App., 26a), and which further stated that,

> Assuming Bank shall . . . succeed to the rights, obligations, properties, assets, investments, deposits, agreements and trusts of the [Failed] Bank . . ., *all to the same extent as though the Assuming Bank had originally assumed the same* . . . .

(Pet.App., 26a-27a) (emphasis added).

Analyzing these contractual provisions under California law, the Court of Appeal concluded that no assignment of priority rights had occurred. It held that "it is essential to the assignment of a right that the assignor manifest an intention to transfer the right." (Pet.App., 13a). In this case, however:

> the opposite intent is manifested by the provision that the assignment of the failed bank's trust assets was made 'to the same extent as though' [Petitioner] 'had originally assumed' those assets from the failed banks, without any involvement by the FDIC. (Rest.2d Contracts, § 203, subd. (c) ['specific terms and exact terms are given greater weight than general language']; *Furtado v. Metropolitan Life Ins. Co.* (1976) 60 Cal.App.3d 17, 25.)

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[2] The agreement also acknowledged that Petitioner was "acquir-[ing] certain assets of, and assum[ing] the deposit and certain liabilities of, the Failed Bank," *not* the FDIC. (Pet.App., 23a).

Id. "Since the parties have demonstrated their ability to draft an assignment with specificity, and since the equities of this case do not favor a finding of implied assignment," the Court of Appeal declined Petitioner's invitation to imply an assignment of priority rights. (Pet.App., 14a).

On the face of the agreement, there is no basis to conclude that Petitioner was ever intended to assume a priority superior to competing creditors. Petitioner was simply to succeed to the same rights as if it had been the original trustee of the Muni-GIC. The Court of Appeal ultimately held that "the fleeting presence of the FDIC in the chain of possession of the Muni-GICs now owned by NationsBank . . . did not transmogrify the Bank['s] claims into claims of the United States government." (Pet.App. 14a). It is only the historical accident of the original trustee's failure that now allows Petitioner to attempt the "alchemy" of converting a private claim into a governmental one.

REASONS FOR DENYING THE PETITION

I. THERE IS NO CONFLICT BETWEEN THIS CASE AND DECISIONS INVOLVING IMPLIED ASSIGNMENT OF STATUTORY RIGHTS THAT CONGRESS SPECIFICALLY GRANTED UNDER FIRREA

Contrary to Petitioner's view, there is no conflict between the Court of Appeal's decision and the decisions of other federal and state courts. Seizing on a sentence in the Court of Appeal's opinion (while ignoring the Court of Appeal's overall rationale), Petitioner seeks to manufacture a conflict by reference to case law specifically distinguished in the decision below. Petitioner tries to argue that cases finding implied assignment of rights created by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA"), Pub. L. No. 101-73, 103 Stat. 183 somehow conflict with the decision below. (Pet., 9-10). In fact, the Court of Appeal's holding does nothing of the sort. It ruled merely that there was no assignment of federal priority rights by 'im-

plication" where the express terms of the contract, public policy and the equities all indicated otherwise. It held nothing more, and held nothing that would cause the consequences that Petitioner fantasizes.

The Court of Appeal's analysis began by reviewing the specific language in the purchase and assumption agreement. It quoted the agreement's provisions of assignment transferring "to the Assuming Bank, all right, title and interest of the Receiver *in and to all of the following assets of the* [*Failed*] *Bank*," and providing that the "Trust Business" was "succeed[ed] . . . *all to the same extent as though the Assuming Bank had originally assumed same* . . . ." (Pet.App., 13a). In this context—reviewing the express words of the agreement—the Court explained that "[i]n neither agreement is there an assignment of *anything* belonging to the FDIC." (Pet.App., 13a). The Court of Appeal then determined that,

> Nothing in the purchase and assumption agreement[] establishes or even suggests an intent by the FDIC to assign to the Bank[] a right belonging to the FDIC qua FDIC. Quite the opposite intent is manifested by the provision that the assignment of the failed bank's trust assets was made 'to the same extent as though' NationsBank . . . 'had originally assumed' those assets from the failed bank[], without any involvement by the FDIC.

(Pet.App., 13a). In short, the Court of Appeal specifically referred to the language governing the trust assets and the express terms of the purchase and assumption agreement, and held that, on this contract and on these equities, any assignment of any FDIC priority rights must be express and would not be implied. The Court of Appeal did *not* rule on the assignment of the statutorily-conferred secret agreement[3] or statute of limitations[4]

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[3] 12 U.S.C. § 1823(e); *D'Oench, Duhme & Co. v. F.D.I.C.*, 315 U.S. 447 (1942).

[4] 12 U.S.C. § 1821(d)(14); 28 U.S.C. § 2415(a).

provisions of FIRREA.[5]

The Court of Appeal distinguished the "secret agreement" cases that originated in *D'Oench, Duhme & Co. v. F.D.I.C.*, 315 U.S. 447 (1942). It specifically considered Petitioner's main case supporting its *D'Oench, Duhme* theory, *Bell & Murphy & Assoc. v. InterFirst Bank Gateway*, 894 F.2d 750, 754 (5th Cir. 1990), and noted that the *D'Oench, Duhme* rule, codified by FIRREA as 12 U.S.C. § 1823(e), may bar claims and defenses against the FDIC based on secret or unrecorded agreements if such agreements would defeat or diminish the FDIC's rights in the acquired asset. The Court below, however, differentiated between this doctrine and federal priority:

> The *D'Oench, Duhme* doctrine . . . may sometimes be extended to benefit the FDIC's assignees (*Cadle Co. II, Inc. v. Lewis*, (Kan. 1993) 864 P.2d 718, 720-721). But the doctrine has never been applied

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[5] Petitioner spends a good deal of time quibbling with the Court of Appeal's construction of the various provisions of their contract. (Pet., 22). These arguments—fact specific as they are—present no basis for certiorari. In any event, Petitioner's arguments are incorrect. Indeed, the FIRREA statute itself tracks the interpretation of the Court of Appeal. In detailing which assets may be transferred by the FDIC as receiver to the bridge bank, the statute provides that a bridge bank may "purchase such assets (including assets associated with any trust business) *of such [failed] bank or banks* . . . as the [FDIC] may, in its discretion, determine to be appropriate." 12 U.S.C. § 1821(n)(1)(B)(ii). The statute provides no authority for the sale of any purported FDIC priority rights, and no basis to assume that any such rights which may exist have been assigned. Petitioner's citation (Pet., 23, and 24, n.8) to *NCNB Texas National Bank v. Cowden*, 895 F.2d 1488 (5th Cir. 1990) is misdirected. There is no dispute that the FDIC, as receiver, took the failed bank's assets by operation of law under FIRREA and specifically 12 U.S.C. § 1821(d)(2)(A)(i). *Cowden* simply stands for the proposition that since the Receiver took the trusts by operation of law, there is no need to have individual appointments of successor trustees on each trust. *Cowden* is in no way inconsistent with the Court of Appeal's conclusion that the agreement failed to assign any priority rights.

> in the manner suggested by NationsBank . . ., which would create an *implied assignment bestowing upon an assignee of the FDIC a governmental priority over other claimants* . . . . Since the parties have demonstrated their ability to draft an assignment with specificity, and since the equities of this case do not favor a finding of implied assignment, we decline the Bank['s] invitation to extend the *D'Oench, Duhme* doctrine.

(Pet.App., 14a) (emphasis added). The Court below did not opine that *D'Oench, Duhme* rights were unassignable, or that such rights were not assigned here. It addressed just the priority issue, and held simply that given the language of the purchase and assumption agreement and the inequity of clothing the bank's claims with "the aura of a governmental entity" merely because of the FDIC's "ephemeral involvement" with the bank (Pet. App., 4a), no *priority* rights would be deemed assigned by implication.

The Court of Appeal also distinguished the cases that had held the FDIC's extended statute of limitations assignable, explaining that the justification for finding assignment of the statute of limitations did not apply here:

> The availability of a longer period of limitations in an action between an assignee of an insolvent bank and a debtor of the same bank does no more than extend the period during which those parties can litigate their rights vis-á-vis each other. There are miles to go before reaching the Bank['s] conclusion, which would permit the assignee of a failed bank to claim priority in an action involving parties who had no relationship at all with the failed bank and who, by pure chance, are attempting to collect from the same third party debtor as the Bank[]. (See also *S.E.C. v. Albert & Maguire Sec. Co., Inc.*, 560 F.2d 569, 573 (3d Cir. 1977) [bank receiving assignment of customer's priority claim in Securities Investor Protection Act liquidation could not assume

> preferred status because it would result in an "inequitable distribution" of the estate].)

(Pet.App., 12a, n.8). The Court below had no cause to decide whether the statute of limitations had been assigned by NationsBank. It decided merely that any right to priority would not be deemed assigned by implication, given the inequity of doing so and the policy considerations that differentiate federal priority issues from those relating to the statute of limitations.[6]

The Court of Appeal's decision is solidly supported by this Court's recent decision in *O'Melveny & Myers v. F.D.I.C.*, 512 U.S. ——, 114 S. Ct. 2048 (June 13, 1994)[7] and other federal decisions refusing to imply rights not expressly granted under FIRREA's statutory scheme. Through the comprehensive FIRREA statute, Congress expressly supplied the FDIC with certain "special" rights, including an extended statute of limitations (12 U.S.C. § 1821(d)(14)) and protection against unwritten or secret agreements that could diminish the FDIC's recovery (12 U.S.C. § 1823(e)). See *O'Melveny*, 114 S. Ct. 2054. Congress deemed each of these rights of sufficient import to warrant augmented power for the FDIC. Some cases, referred to by Petitioner, have found that the same policy rationale motivating Congress to supply the FDIC with such powers sufficiently supports

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[6] Similarly, Petitioner's invocation of *Tivoli Ventures, Inc. v. Bumann*, 870 P.2d 1244 (Colo. 1994) (Pet. 14, 20-21) and *Fall v. Keasler*, 1991 WL 340182 (N.D. Cal. 1991) (Pet. 16, 20), is to no avail. The fact that these courts found that assignees of the FDIC as receiver were entitled to assert the statutorily-extended federal agency statute of limitations does not establish that the language of the purchase and assumption agreements assigns the federal priority to Petitioner. Further, *Fall v. Keasler* is an unpublished United States District Court opinion, without precedential value.

[7] See the more detailed discussion of *O'Melveny in* Part II.A., *infra*, at 12-14.

the FDIC's assignment of such powers. The Petition wrongly contends that there is an inconsistency between those FIRREA-based cases and the Court of Apeal's "refusal to extend" these doctrines to find an "implied assignment" of priority rights *not* created or authorized by FIRREA. (See, *e.g.*, Pet., 17).

Congress was aware of the issue of whether or not the FDIC is entitled to governmental priority at the time it enacted FIRREA. See *PIMA Financial Service Corp. v. Intermountain Home Systems, Inc.*, 786 F. Supp. 1551, 1560 (D. Colo. 1992). But rather than extend the governmental priority statute to the FDIC—as it extended the *D'Oench, Duhme* doctrine by enactment of 12 U.S.C. § 1823(e)—Congress has repeatedly declined to afford the FDIC full-fledged government status and priority rights. Congress has never enacted any statute affording the FDIC the right to governmental priority. As *O'Melveny* and *Pima* make clear, Congress' decision not to afford the FDIC express priority powers demarks the limits for the implication of special powers.[8] In *O'Melveny's* words, *"inclusio unius, exclusio alterius."* 114

[8] The federal courts have also recognized the tension between claims of the *FDIC* in insolvency proceedings and the claims of other creditors, and have therefore "limited the applicability of *D'Oench, Duhme* in bankruptcy proceedings." *Texas Trust Savings v. Nasr (In re Nasr)*, 120 B.R. 855, 859 (Bankr. S.D. Tex. 1990) (despite *D'Oench, Duhme* and federal holder in due course doctrines, debtor could assert bank official's alleged fraud in defense to a FSLIC assignee's action to determine dischargability); see also *In re Still*, 963 F.2d 75 (5th Cir. 1992) (rejecting FDIC's claim that its vital role in banking system necessitated "special protections," and holding that where FDIC opposed other unsecured creditors in action to recover preferential transfer, "the FDIC deserves no greater priority than these other creditors," and that "there is no indication . . . that Congress intended the FDIC to receive a similar priority here"); *In re Pernie Bailey Drilling Co.*, 111 B.R. 565, 576 (Bankr. W.D. La. 1990) (the FDIC as receiver is not automatically a good faith transferee for value under Section 550(b)).

S. Ct. at 2054. FIRREA "places the FDIC in the shoes of the insolvent S&L, to work out its claims under state law, except where some provision in the extensive framework of FIRREA provides otherwise." *Id.*; *PIMA*, 786 F. Supp. at 1560. Indeed, no published decision has ever held that the FDIC may assign a right of governmental priority. The Court of Appeal's distinction between implied assignment of priority rights and implied assignment of FIRREA power tracks the distinction drawn in *O'Melveny*. The Court of Appeal properly declined to find an implied assignment of priority rights here.[9]

II. NOTHING IN THIS CASE WARRANTS DISPLACEMENT OF THE STATE LAW RULE OF DECISION BY THE CREATION OF FEDERAL COMMON LAW

Even assuming that there was some conflict between the decision below and those in other jurisdictions, which there is not, that assumption would not justify certiorari. A conflict between state laws—even a divergence from the majority of jurisdictions—provides no basis for displacing a state's rule with a federal one. See *O'Melveny*, 114 S. Ct. at 2053 (refusing to create federal common law

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[9] Petitioner's assertion that there is a uniform body of precedent supporting its claim on assignability of priority rights is merely an attempt to stitch together various holdings and rationales of different opinions to create a rule of law which does not exist. Notwithstanding Petitioner's claims, the collection of cases it relies upon are distinguishable because they do not address federal priority rights or any rights other than those expressly provided for in FIRREA. They merely hold that certain protections expressly granted the FDIC may be enforced.

Finally, Petitioner's assertion that "the right to assert the FDIC's priority in a liquidation is markedly less intrusive" (Pet., 17) than *D'Oench Duhme* and statute of limitations rights is wrong. Placing Petitioner ahead of all other policyholders would directly impact the ELIC Plan of Rehabilitation and interfere with substantial state interests in regulating insurance insolvencies by elevating its priority over and above identical competing claims. See *infra*, at 18-19.

despite state law's divergence from "the vast bulk of decisions from 43 jurisdictions"). State law, not federal common law, would still control.

A. Federal Law Does Not Apply Because This Private Dispute Between Non-Federal Parties Does Not Directly Affect The Interests Of The United States Government

Cases warranting the creation of special federal law are " 'few and restricted,' " limited to areas where there is a " 'significant conflict between some federal policy or interest and the use of state law.' " *O'Melveny*, 114 S. Ct. at 2055 (quoting *Wheeldin v. Wheeler*, 373 U.S. 647, 651 (1963); *Wallis v. Pan American Petroleum Corp.*, 348 U.S. 63, 68 (1966)). No such conflict exists here.

In *O'Melveny*, the FDIC sued a law firm for professional negligence related to the failure of a savings and loan called ADSB. The firm defended on the ground that, under California law, the knowledge of ADSB's officers must be imputed to ADSB, and hence to the FDIC acting as receiver, and that such knowledge barred the FDIC's professional negligence claim. The FDIC contended that federal law preempted application of the imputation defense to the receiver, arguing that federal law governs questions involving rights of the United States arising under nationwide programs. This Court held,

> What is fatal to respondent's position in the present case is that it has identified no significant conflict with an identifiable federal policy or interest. There is not even at stake that most generic (and lightly invoked) of alleged federal interests, the interest in uniformity. The rules of decision at issue here do not govern the primary conduct of the United States or any of its agents or contractors, but affect only the FDIC's rights and liabilities, as receiver, with respect to primary conduct on the part of private actors that has already occurred. Uniformity of law might

> facilitate the FDIC's nationwide litigation of these suits, eliminating state-by-state research and reducing uncertainty—but if the avoidance of those ordinary consequences qualified as an identifiable federal interest, we would be awash in 'federal common-law' rules.

Id. Having rejected the same "uniformity" argument suggested by Petitioner here (see, *e.g.*, Pet., 16, 17), *O'Melveny* further rejects Petitioner's argument that, absent application of a federal rule, public funds available to rescue insolvent banks will be "depleted." (See, *e.g.*, Pet., 27-28).

> [N]either FIRREA nor the prior law sets forth any anticipated level for the [deposit insurance] fund, so what respondent must mean by 'depletion' is simply the forgoing of *any* money which, under any *conceivable* legal rules, might accrue to the fund. That is a broad principle indeed, which would support not just elimination of the defense at issue here, but judicial creation of new, 'federal-common-law' causes of action to enrich the fund. Of course we have no authority to do that, because there is no federal policy that the fund should always win. Our cases have previously rejected 'more money' arguments remarkably similar to the one made here.

Id. (citations omitted). Thus, *O'Melveny* has already rejected the "uniformity" and "more money" arguments advanced by the Petitioner for creation of federal common law respecting FDIC activities as receiver.

In any event, the Petition's footnote purporting to explain why federal law should apply relies on cases in circumstances where federal law was applied to contracts of the United States, in litigation to which the United States was a party. (Pet., 22, n.7). Those cases are inapplicable here, in the first instance, because the purchase and assumption agreement was not entered into by the United States. As *O'Melveny* stated, "the FDIC is

not the United States, and even if it were, we would be begging the question to assume that it was asserting its *own* rights rather than, as receiver, the rights of [the failed bank]." *Id.* at 2053. *A fortiori,* the bridge bank created by the FDIC to transfer assets to Petitioner was not the United States. Unless this Court is prepared, six months after *O'Melveny,* to reverse field and hold the purchase and assumption agreement to be a contract entered by the United States, there is no contract of the United States to which rules of federal construction could even possibly be applied.[10]

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[10] The authorities relied upon by the Petition are easily distinguishable because the United States was a party to those contracts and because the United States was a party to the lawsuits interpreting them. *United States v. Seckinger,* 397 U.S. 203 (1970) (suit by United States requiring interpretation of indemnification term of standard form government procurement contract promulgated by regulation issued by General Services Administration); *United States v. County of Allegheny,* 322 U.S. 174 (1944) (action involving state taxation of machinery installed in contractor's mill pursuant to contractual requirements of United States for production of ordinance); *Clearfield Trust Co. v. United States,* 318 U.S. 363 (1943) (action involving forged endorsement on United States Treasury check; disbursement of United States funds and payment of debts governed by federal law); *United States v. Tharp,* 973 F.2d 619 (8th Cir. 1992) (interpretation of guarantee agreement between borrower's principals and SBA governed by federal law); *Grosinsky v. United States,* 947 F.2d 417 (9th Cir. 1991) (action against United States under Federal Tort Claims Act for negligence and tortious breach of contract arising out of failure of vasectomy); *United States v. Triple A Machine Shop, Inc.,* 857 F.2d 579 (9th Cir. 1988) (ejectment action against lessee of government property; federal law governs interpretation of government lease contract). Further, *Dababneh* and *Downriver* are inapplicable because those two cases merely applied federal law to the distribution of assets of insolvent federal banks under federal insolvency law, and did not construe the rights of the insolvent bank itself against a third party. *Dababneh v. FDIC,* 971 F.2d 428 (10th Cir. 1992) (suit by landlord with rejected lease alleging nonratable distribution in violation of National Bank Act; federal law governs amount of proof necessary to establish validity of claims against bank's receiver); *Downriver Com. Fed. Credit U.*

Even if this case did involve a contractual obligation of the United States, which it does not, that fact would not require creation of federal law. State law governs where litigation involving federal contracts "is purely between private parties and does not touch the rights and duties of the United States." *Bank of America v. Parnell,* 352 U.S. 29, 33 (1956). Where a case involving non-federal litigants "will have no direct effect upon the United States or its Treasury," there is no cause for application of federal law. *Miree v. Dekalb County, Ga.,* 433 U.S. 25, 29 (1977). And, although any federal transaction necessarily "radiates interests in transactions between private parties," the possibility that some private dispute may have indirect ramifications on the federal government is insufficient to support displacement of state law. *Parnell,* 352 U.S. at 33-34.

In *Miree,* for example, victims of an airplane accident sued a Georgia county airport. They claimed that federal common law governed their status as third party beneficiaries under a federal contract by which the county agreed with the FAA to maintain in non-hazardous conditions the areas surrounding the airport. 433 U.S. at 28, 30. Despite the presence of a government contract, this Court declined to apply federal law, expressly distinguishing the *Seckinger* and *Clearfield Trust* line of cases. "Since only the rights of private litigants are at issue here, we find the *Clearfield Trust* rule inapplicable." 433 U.S. at 30. The *Miree* court held insufficient plaintiffs' assertion of a federal interest in uniformity and certainty of interpretation of FAA contracts. *Id.* "Nor is the fact that the United States has a substantial interest in regulating aircraft travel and promoting air travel safety sufficient, given the narrow question before us, to

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v. Penn Square Bank, 879 F.2d 754 (10th Cir. 1989) (action by depositors fraudulently induced to deposit funds in insolvent bank seeking recovery of total versus pro rata share of assets; federal law governs distribution of failed bank's assets).

call into play the rule of *Clearfield Trust.*" *Id.* at 31. As in *Miree,* only the rights of private parties are at issue here. The fact that the United States may have an interest in bank regulation does not support creation of a federal common law, given the narrow question here of implied assignment of priority rights in a state-regulated insurance insolvency.

In *Bank of America v. Parnell, supra,* the Court held an endorser's good faith in cashing stolen federal bonds was a question of state law where litigated between private parties. It found insufficient the contention that "floating of securities by the United States might somehow or otherwise be adversely affected by the local rules of a particular state regarding the liability of a converter." 352 U.S. at 33. "This is far too speculative, far too remote a possibility to justify the application of federal law" to such transactions. *Id.* at 33-34.

Similarly, in this case, the asserted risk to the federal fisc is remote and speculative at most. As to past sales of bank assets, the amount the FDIC will receive has already been determined and will remain unaffected by this case. As to sales of assets in the future, it is exceedingly improbable that the purchase price would turn on whether federal priority rights are deemed assigned by implication.[11] As explained in Part III, *infra,* the law is that the FDIC is not entitled to priority in its own right. In determining what purchase price to offer, a purchasing party could not depend on an implied assignment of priority rights that are dubious at best. But even if the purchaser would pay more for an assignment of whatever rights the FDIC might have, delivery of any such rights could be easily accomplished simply by including an express and unambiguous assignment of specific FDIC

[11] Certainly the Petition does not provide any factual support for its assertion that the prices paid for failed bank assets will be affected in any manner by this decision.

rights. There is no need for the Court to create federal common law to protect the public fisc.

This very conclusion was reached in *Wallis v. Pan American Petroleum Corp.*, 384 U.S. 63 (1966). There, assignees of federal oil leases sought to impose federal common law to interpret their lease assignments and thereby displace a Louisiana state law that assignment of such leases must be in writing. This Court reversed the Fifth Circuit's conclusion that the Louisiana law thwarted the policy of 30 U.S.C. § 187(a), which provided that oil and gas leases shall be assignable. See 384 U.S. at 69. The "guiding principle is that a significant conflict between some federal policy or interest and the use of state law must be shown." *Id.* "[H]owever fitting [imposition of federal common law] may be where a State interposes unreasonable conditions on assignability, it can have no force in this instance because Louisiana concededly provides a quite feasible route for transferring any mineral lease or contracting to do so, namely, by written agreement." *Id.* at 69-70. The same rationale supports application of state law here. State law merely requires that any assignment of governmental priority rights be express rather than implied—a requirement that does not conflict with any federal policy. Any party wishing to transfer priority rights may quite feasibly do so by a contract expressly saying so.[12]

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[12] In *Boyle v. United Technologies Corp.*, 487 U.S. 500, 507 (1988), the Court used federal common law to immunize government defense contractors from liability to private parties where the state-imposed duty of care was "precisely contrary to the duty imposed by the government contract." 487 U.S. 509. *Boyle* relied on the fact that the United States would be "directly affected" because, due to the nature of the defense industry, "the financial burden of judgments against the contractors would ultimately be passed through, substantially if not totally, to the United States itself." *Id.* at 507, 511-12. *Boyle* thus differs from this case due to (1) the direct (and unavoidable) conflict between federal contracts and state tort law, and (2) the direct effect upon the federal fisc.

Moreover, because the regulation of insurance insolvencies is entrusted to the states through the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-15, the states have a strong interest in application of state law to priority determinations. Under the McCarran-Ferguson Act, the business of insurance is subject to the laws of the states, which hold the authority to operate state systems for the regulation, taxation, and insolvencies involving the business of insurance. 15 U.S.C. § 1012.[12] The states have the exclusive right and duty to rehabilitate or liquidate insurance companies and have enacted comprehensive regulatory schemes which include provisions for insolvency. See, *e.g.*, California Insurance Code §§ 1010-1063. As one federal court has expressed:

> Since these schemes are designed to protect the interests of policyholders and to provide for the adjustment of the rights of creditors and policyholders in the event of insolvency, Congress in enacting [McCarran-Ferguson] decided that liquidation of insurance companies should be left to the states . . . . By preserving state liquidation proceedings, Congress sought to prevent bankruptcy or reorganization courts from interfering with comprehensive state insurance regulations and with the rights of insureds protected by such regulations.

In re Equity Funding Corp. of America, 396 F. Supp. 1266, 1275 (C.D. Cal. 1975); see also *Baldwin-United Corp. v. Garner*, 678 S.W. 2d 754 (Ark. 1984), *cert. den.*, 471 U.S. 1111 (1985).

This Court recently affirmed the recognition of states' interests in priority issues in insurance insolvencies in *U.S. Department of Treasury v. Fabe*, 508 U.S. ——, 113 S. Ct. 2202 (1993). *Fabe* held that the general federal priority statute 31 U.S.C. § 3713 did not preempt

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[13] See also, *SEC v. National Securities, Inc.*, 393 U.S. 453 (1969); *Wilburn Boat Co. v. Fireman's Fund Ins. Co.*, 348 U.S. 310 (1946); *Prudential Ins. Co. v. Benjamin*, 328 U.S. 408 (1946); *Allstate Ins. Co. v. Lanier*, 361 F.2d 870 (4th Cir. 1966), *cert. denied*, 385 U.S. 930 (1966).

a state satute governing priorities for policyholders in insurance insolvencies, because the state priority statute entails the "business of insurance" within the meaning of the McCarran-Ferguson Act. In *Fabe*, the conflict between the federal priority statute and the state priority statute was resolved in favor of the state statute: the priority of policyholders superior to the federal government was maintained.

The State of California has a vital interest in resolving the ELIC insolvency and rehabilitation, and in protecting the thousands of policyholders concerned in this matter. These interests fairly support the Court of Appeal's decision not to imply assignment of priority rights in a manner that would inequitably give one policyholder a windfall at all others' expense.

In short, none of the policy arguments advanced by the Petition warrants creation of federal common law here. This is a dispute between private parties that will not directly affect or conflict with the interests of the United States. State law applies.

B. FIRREA Does Not Authorize A Federal Common Law Rule

O'Melveny specifically disposes of any claim that the policies behind FIRREA serve as a source of federal common law. (See, *e.g.*, Pet., 27). *O'Melveny* rejected a contention, akin to Petitioner's here, that FIRREA "not only did not prevent but positively authorized federal common law." 114 S. Ct. at 2054. The Court refused to "adopt a court-made rule to supplement federal statutory regulation that is comprehensive and detailed; matters left unaddressed in such a scheme are presumably subject to the disposition provided by state law.'" *Id.* The Court stated:

> Respondent argues that [FIRREA] should be read as a *nonexclusive* grant of rights to the FDIC receiver, which can be supplemented or modified by

> federal common law; and that FIRREA as a whole, by demonstrating the high federal interest in this area, confirms the court's authority to promulgate such common law. This argument is demolished by those provisions of FIRREA that specifically create special federal rules of decision regarding claims by, and defenses against, the FDIC as receiver. . . . *Inclusio unius, exclusio alterius.* It is hard to avoid the conclusion that [FIRREA] places the FDIC in the shoes of the insolvent S&L, to work out its claims under state law, except where some provision in the extensive framework of FIRREA provides otherwise. To create additional 'federal common law' exceptions is not to 'supplement' this scheme, but to alter it.

Id. (citations omitted).

After *O'Melveny*, there is no room left for Petitioner's contention that FIRREA's scheme for disposition of failed banks' assets is subject to "supplementation" through a federal common law of implied assignment of priority rights. (See, *e.g.*, Pet., 26).[14] Petitioner's reliance on

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[14] Recent federal court decisions follow *O'Melveny* and fully support the proposition that there is no conflict with federal policy in this case which would justify the creation of federal common law. *Calhoun v. Yamaha Motor Corp.*, —— F.3d ——, 1994 WL 595577 (3rd Cir. 1994); *Resolution Trust Corp. v. Everhart*, 37 F.3d 151 (4th Cir. 1994) (applying state statute of limitations and not federal common law to claims by RTC against former directors and officers of failed federally chartered and federally insured thrift institution); *Beazer East, Inc. v. Mead Corp.*, 34 F.3d 206 (3rd Cir. 1994) (applying state law and not a federal rule of decision in interpreting and construing a contract's indemnification provisions that affect liability imposed under federal statutes); *F.D.I.C. v. Oldenburg*, 34 F.3d 1529 (10th Cir. 1994); *Resolution Trust Corp. v. Forest Grove, Inc.*, 33 F.3d 284 (3rd Cir. 1994); *Resolution Trust Corp. v. Maplewood Ins.*, 31 F.3d 1276 (4th Cir. 1994) (applying a state rule of decision as opposed to the creation of a federal rule of decision in a claim involving holder in due course by RTC on a note of a failed bank); *Resolution Trust Corp.*

pre-*O'Melveny* cases that referred to a federal common law respecting FIRREA-created rights is misplaced. (See Pet., 13-16). Whatever the continuing vitality of those cases might be after *O'Melveny*, it is certainly now settled that FIRREA does not spread a blanket of federal common law covering assignment of priority rights that Congress declined to grant the FDIC in the FIRREA statutes.[15]

In sum, Petitioner fails to provide any reason why this case is one of those extraordinary cases in which the judicial creation of a federal rule of decision is warranted.

III. CERTIORARI SHOULD BE FURTHER DENIED BECAUSE THE FDIC, ACTING AS RECEIVER, IS NOT ITSELF ENTITLED TO HOLD OR ASSIGN THE PRIORITY STATUS OF THE UNITED STATES GOVERNMENT

The Petition should be denied for the independent reason that granting certiorari would be a futile and purposeless act. Addressing the narrow question of whether or not priority rights must be deemed assigned by implication will not end this case. Even if that question were somehow resolved in Petitioner's favor, Petitioner would still not obtain governmental priority because the FDIC, acting as receiver, never had governmental priority rights to assign.

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v. Baker, Civ. No. 93-0093, 1994 WL 637359 (E.D. Pa. Nov. 14, 1994).

[15] The FIRREA statute itself suggests no basis for an implication of assignment of rights belonging to the FDIC. In detailing which assets may be transferred by the FDIC as receiver to the bridge bank, the statute provides that a bridge bank may "purchase such assets (including assets associated with any trust business) *of such [failed] bank or banks* . . . as the [FDIC] may, in its discretion, determine to be appropriate." 12 U.S.C. § 1821(n)(1)(B)(ii) (emphasis added). The statute provides no authority for the sale of any purported FDIC priority rights, and no basis to assume that any such rights which may exist have been assigned.

A. The FDIC Does Not Receive Governmental Priority Powers When Acting As Receiver Under FIRREA

The Court of Appeal stated its inclination to rule that the FDIC was not entitled to governmental priority, but nonetheless decided not to address that issue. (Pet.App., 11a). The correctness of the Court's "inclination" has been affirmed by this Court's *O'Melveny* decision. As noted above, *O'Melveny* stated that "the FDIC is not the United States, and even if it were we would be begging the question to assume that it was asserting its own rights rather than, as receiver, the rights of ADSB." *O'Melveny*, 114 S. Ct. at 2053. On the question of the status of the FDIC while acting as receiver, this Court has answered that "the FDIC as receiver 'steps into the shoes' of the failed S&L . . . obtaining the rights of the insured depository institution that existed prior to receivership.'" *Id.* at 2054.[16] Finally, as noted above, *O'Melveny* explained that the FDIC possesses no special federal rights as receiver beyond those expressly provided under FIRREA. *Id.* at 2055. Since FIRREA had enumerated certain special rights for the FDIC as receiver, the failure to include priority rights forecloses their application.

For these reasons, the FDIC had no priority rights to assign to Petitioner. The majority and better reasoned of the pre-*O'Melveny* cases so held.[17] *O'Melveny* eliminates

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[16] See also, *F.D.I.C. v. Wheat*, 970 F.2d 124, 130 (5th Cir. 1992); *Trigo v. F.D.I.C.*, 847 F.2d 1499, 1502 (11th Cir. 1988); *Royal Bank Export Finance Co. v. Bestways Dist. Co.*, 280 Cal. Rptr. 355 (1991); *F.D.I.C. v. State of New York*, 718 F. Supp. 191 (S.D.N.Y. 1989), *aff'd*, 928 F.2d 56 (2d Cir. 1991).

[17] Prior to the *O'Melveny* decision, only a few courts had considered the issue of the entitlement of the FDIC to claim priority under 31 U.S.C. § 3713. Only one of those cases, *In re Big D' iscount Stores, Ltd.*, 2 B.C.D. 1073 (Bankr. D.S.C. 1976), held that the FDIC could assert the federal priority. However, that case failed to consider the issue of federal funding of the FDIC, an essential factor in analyzing whether it is entitled to federal priority. Moreover, this case has never been followed by any other court. *Lapadula & Villani, Inc. v. United States*, 563 F. Supp. 782 (S.D.N.Y. 1983)

any remaining uncertainty as to the FDIC's lack of governmental status when acting in the role of receiver of a failed institution.

B. The Government's Priority Rights Are Not Assignable In Any Event

Taking this to the next level, which is necessary because Petitioner is an assignee, under the case law, Petitioner is not entitled to priority by assignment. Petitioner's claim of assigned priority actually conflicts with ap-

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was described as the "leading case on the issue" by the court in *PIMA Financial Service Corp. v. Intermountain Home Systems, Inc.*, 786 F. Supp. 1551 (D. Colo. 1992). The *Lapadula* Court denied extension of the federal priority to the FDIC, finding that public funds were unaffected by its ability to recover debts owed to it as successor to claims of an insolvent bank, stating that "the FDIC is not an integral part of the governmental mechanism but is rather a separate legal entity serving essentially a proprietary rather than a sovereign function." 563 F. Supp. at 784.

Prior to *O'Melveny*, the leading case on this subject was *PIMA*, which contains a comprehensive analysis of the entitlement of the FDIC to the federal priority. The *PIMA* court noted that the FDIC's banking-related activities are privately funded under FIRREA. 786 F. Supp. at 1558. Further, the Court found that (i) Congress did not give the FDIC "full-fledged agency status" in amending the FDIC's powers under the Federal Deposit Insurance Act, (ii) Congress did not grant the FDIC the federal priority, as it had done with other quasi-governmental institutions, and (iii) an analysis of the legislative history of FIRREA suggests that "the FDIC cannot take advantage of certain priorities normally afforded to the federal government." *Id.* at 1560-61. As a result, the Court found that the FDIC was not entitled to assert the federal priority of 31 U.S.C. § 3713.

Acting as receiver, the FDIC obtained only the rights of the failed bank in this case. Petitioner acknowledges the purchase and assumption agreement to which the Bank traces its purported rights is an agreement between the FDIC, as receiver of the failed bank, and the bridge bank. (Pet., 4). *O'Melveny, Lapadula,* and *PIMA* thus make it clear that the FDIC, acting as receiver of a failed bank, is not the federal government and is not entitled to any special priority rights where none were provided for it in FIRREA.

plicable case law. Courts refuse to recognize transfers of the government's priority rights by subrogation or assignment, especially when recognition of such rights would produce an inequitable result under applicable law. See *S.E.C. v. Albert & Maguire Sec. Co., Inc.*, 560 F.2d 569, 573 (3d Cir. 1977) (bank receiving assignment of a customer's priority claim in Securities Investor Protection Act liquidation could not assume preferred status because "it would result in an inequitable distribution of the bankrupt estate, inconsistent with the Congressional purpose" of that Act); *In re Int'l Eng'rs, Inc.*, 58 B.R. 1005, 1006-07 (Bankr. S.D. N.Y. 1986) (customs broker that voluntarily paid debtor's tax obligation was not entitled to governmental priority against bankrupt estate); *In re Tygrett*, 72 B.R. 129, 130-31 (Bankr. C.D. Ill. 1987) (same).

Petitioner has obviously futilely searched for legal support for the proposition that an assignee of the *United States* is entitled to statutory priority under 31 U.S.C. § 3713. It is equally obvious that there is none. For example, Petitioner claims that *Bramwell v. United States Fidelity & Guaranty Co.*, 269 U.S. 483 (1926), stands for the "broader proposition that [a private party] was entitled to assert the government priority as assignee of the government." (Pet., 20). That is not the holding of *Bramwell*. In *Bramwell*, a surety was permitted to assert the government's priority because they had paid a claim on the government's behalf. 269 U.S. at 486. The surety's priority did *not* derive from the assignment, but rather from a specific statute (R. S. § 3468), which provided:

> *Priority of Sureties.* Whenever the principal in any bond given to the United States is insolvent . . . and . . . any surety on the bond . . . pays to the United States the money due on such bond, *such surety . . . shall have the like priority for the recovery and receipt of the moneys . . . as is secured to the United States . . .*

(quoted in *Barnett v. American Surety Co. of New York*, 77 F.2d 225, 226 (10th Cir. 1935) (emphasis added)). No such statute is at issue here. In fact, this Court rejected Petitioner's precise argument in *Nathanson v. N.L.R.B.*, 344 U.S. 25 (1952) where it held that *Bramwell* would not support the collection of a priority claim by the United States for the benefit of a private party. 344 U.S. at 28.[18]

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[18] Petitioner's reliance on *Small Business Administration v. McClellan*, 364 U.S. 446 (1960) to suggest that federal policy considerations upholding a priority claim under 31 U.S.C. § 3713 is also misplaced. (Pet., 21-22). In *McClellan*, the SBA and a private bank jointly loaned a debtor $20,000, agreeing that any collections on the loan would be shared 75%/25% based upon the amount loaned by each party. *Id.* at 447. When the borrower filed for bankruptcy, the SBA asserted statutory priority for its *own* $15,000 loan; *no priority* was asserted for the $5,000 loaned by the bank. For this Court, the key issue was whether *Nathanson* suggested that the SBA "forfeited any right it might otherwise have had to priority by agreeing to turn over to the bank one fourth of any distribution obtained because of its priority." *Id.* at 451. This Court rejected this reading of *Nathanson* because "the money (*i.e.* the SBA's $15,000) was loaned by, and the debt sought to be collected is due to, the United States." *Id.* A parity of reasoning suggests that a claim of priority for the $5,000 loan by the private bank would not have survived a challenge under *Nathanson*; indeed, the court so held in *W.T. Jones & Co. v. Foodco Realty, Inc.*, 318 F.2d 881, 889 (4th Cir. 1963). Petitioner's similar claim here—that it may assert a priority against the ELIC estate on its own account, for the benefit of the bondholders—is irreconcilable with *Nathanson* and *W.T. Jones*, and should be rejected by this Court.

CONCLUSION

For the reasons set forth above, the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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